



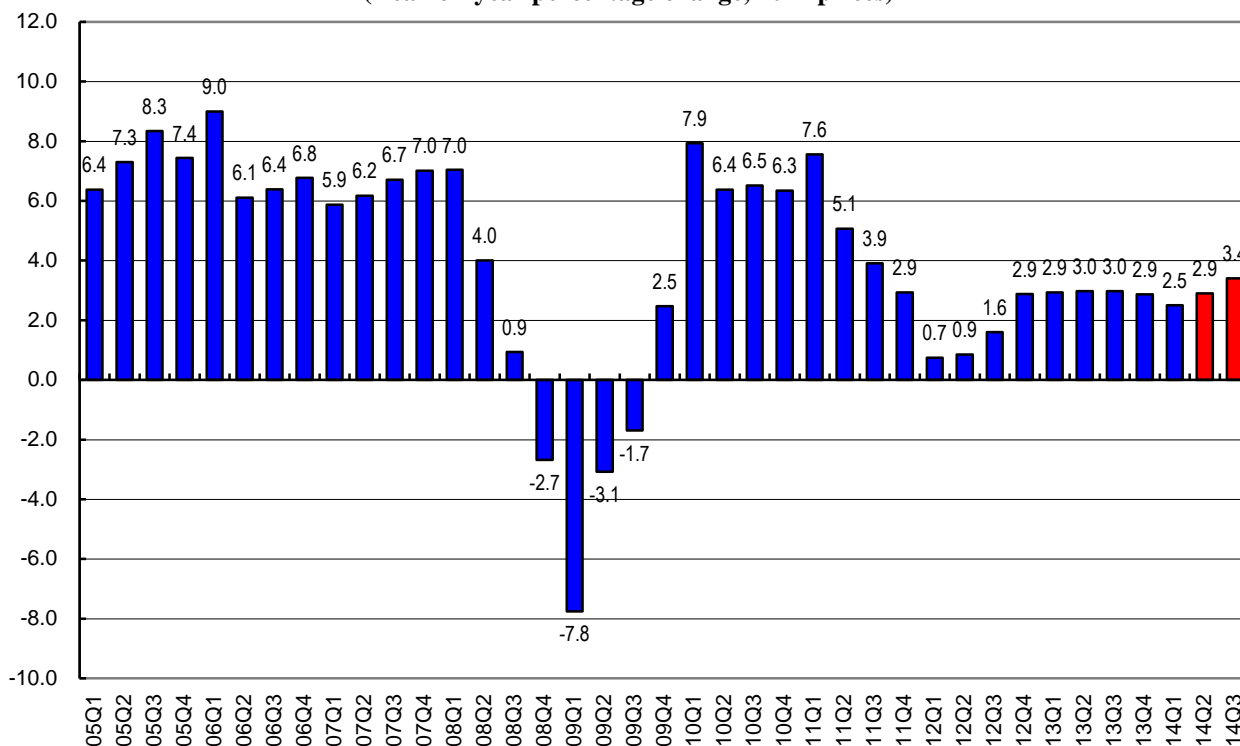
HKU Announced 2014 Q3 HK Macroeconomic Forecast

July 3, 2014

Hong Kong Economic Outlook

The APEC Studies Programme of the Hong Kong Institute of Economics and Business Strategy at the University of Hong Kong (HKU) released its quarterly Hong Kong Macroeconomic Forecast today (July 3). According to its High Frequency Macroeconomic Forecast, real GDP in 14Q2 is estimated to grow by 2.9% when compared with the same period last year. This is a downward revision from the previous forecast release of 3.7%. This substantial revision mainly reflects the weak external demand caused by the cold winter in the North America. In 14Q3, real GDP growth is forecast to be 3.4% when compared with the same period last year.

Real Gross Domestic Product
(Year-on-year percentage change, 2012 prices)



Professor Richard Wong Yue-Chim, Professor of Economics at HKU said that, "The harsh winter dampened the US economy more than expected in the first quarter of 2014. The deeper-than-expected slump in the US economy translated into a sluggish growth of Hong Kong's external demand in the first quarter of 2014. Nevertheless, we expect the rather strong domestic

demand continues to drive the real GDP growth in the current quarter. Domestic demand is expected to contribute for 2.6 percentage points of growth. The external demand, as measured by the net exports of goods and services, is forecast to contribute only 0.8 percentage points. In aggregate, Hong Kong GDP is forecast to grow by 3.4% in the current quarter."

"The labour market is projected to remain relatively stable with the unemployment rate projected to be flat at 3.2% in 14Q3 as compared to 14Q2. Inflation is expected to be stable in the near term. The headline consumer inflation rate is forecast to 4.0% in the third quarter, up from the estimated 3.7% in the second quarter in 2014," according to Dr. Ka-fu Wong, Principal Lecturer of Economics at HKU.

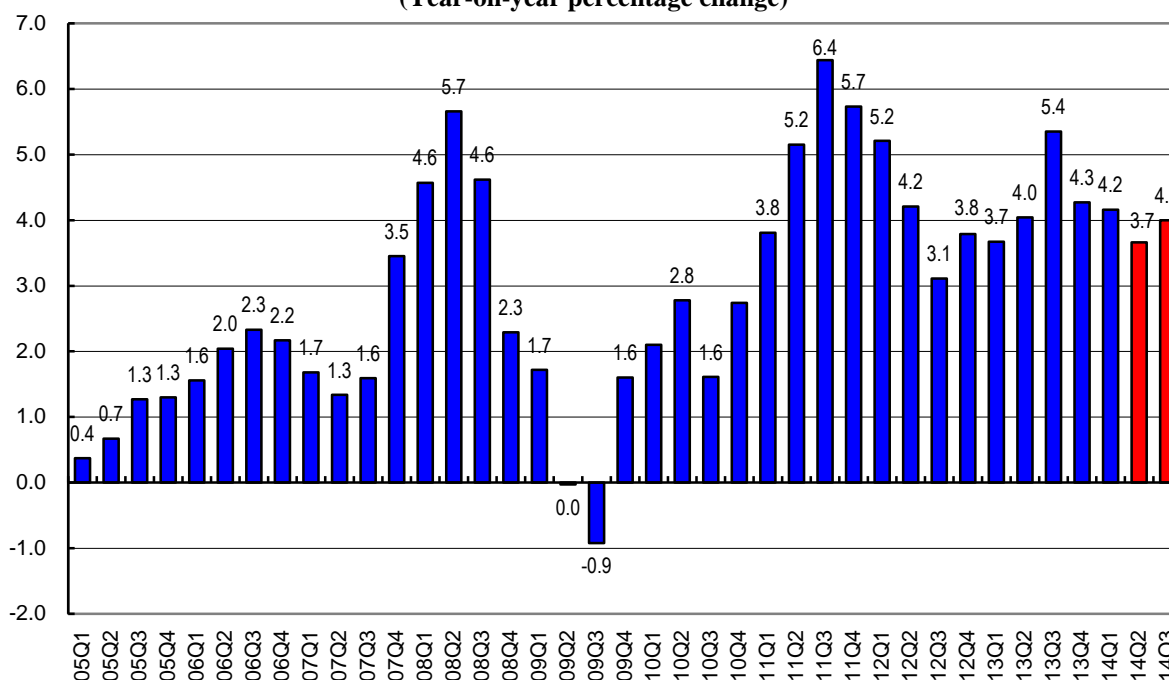
The forecast details are in Table 1 and Table 2, and the forecasts of selected monthly indicators are in Table 3. All growth rates reported are on a year-on-year basis.

Forecast Highlights

- Private consumption spending grew by 2.0% in 14Q1, a slowdown from the 3.6% growth in 13Q4. This slowdown is partly due to a higher base of comparison a year earlier. Given stable job market, private consumption spending is projected to grow in a slightly faster pace at 3.0% in 14Q3, an acceleration from the forecast of 2.2% in 14Q2.
- The volume of retail sales dropped by 9.5% in April 2014. Jewellery category retail sales volume dropped by 37.7%, while food, clothing and other consumer goods recorded 1.9%, 9.6% and 3.4% growth respectively. This decline in retail sales reflected the change in visitor's consumption pattern and a higher base of comparison. Thus, we expect that drop in retail sales will be temporary. We expect the volume of retail sales in 14Q2 to drop by 4.6%, and that in 14Q3 to grow by 2.4%.
- Total exports of goods rose by 0.5% in 14Q1, reflecting the impact of the US harsh winter in 14Q1. In May 2014, Hong Kong's nominal external merchandise exports exhibited a 4.9% growth, reverting from the 1.7% drop in April 2014. Foreign inventory restocking is expected to support the total exports of goods. Total exports of goods are estimated to grow by 2.5% in 14Q2 and are forecast to accelerate to grow by 3.3% in 14Q3.
- Imports of goods grew only by 1.2% in 14Q1, much lower than the 6.1% growth in 13Q4. In May 2014, the nominal imports grew by 3.7%, accelerated from the 2.4% growth in April 2014. We expect the growth of imports of goods to resume. It is forecast to grow by 2.6% in 14Q2 and 3.5% in 14Q3.

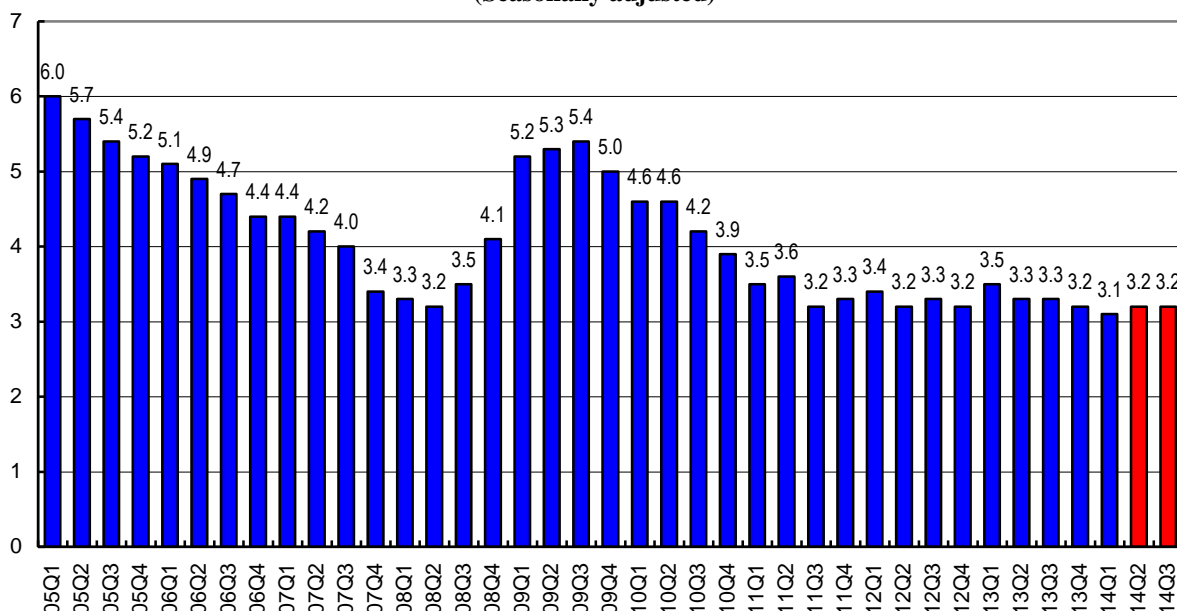
- Service exports grew by 3.1% in 14Q1, decelerating from the 4.7% growth in 13Q4. Growth in visitor arrivals held up well at 10.9% in April 2014. The influx of Mainland visitors is expected to fuel travel related services continuously in the near term. Thus, the service exports are forecast to pick up and grew by 4.4% in 14Q2 and 5.0% in 14Q3.
- Service imports fell by 0.2% in 14Q1, reverting the 5.5% growth in 13Q4. Service imports are forecast to grow by 2.6% and 2.8% in 14Q2 and 14Q3 respectively.
- Gross fixed capital formation rose by 3.0% in 14Q1, slowed from the 5.3% growth in 13Q4. Slack of infrastructural projects commencement is expected to dampen the growth in investment spending. The gross fixed capital formation is projected to fall by 1.4% in 14Q2 and 0.4% in 14Q3.
- Investment in land and construction grew by 4.5% in 14Q1, reverting the 8.6% drop in 13Q4. The investment in land and construction is projected to fall by 0.1% and 1.9% in 14Q2 and 14Q3 respectively.
- Investment spending in machinery, equipment and computer software grew only by 1.4% in the 14Q1, which is a noticeable slowdown as compared to the 17.5% surge in 13Q4. The investment in machinery, equipment and computer software is projected to drop by 2.3% in 14Q2 and grow at 0.7% in 14Q3. The deficient growth performance in recent quarters is partly due to a higher base of comparison a year earlier.

Composite Consumer Price Index
(Year-on-year percentage change)



- The general price level, as measured by the Composite CPI, rose by 3.7% in May 2014. Inflationary pressure is expected to remain relatively stable in the near term. The headline consumer inflation rate is forecast to be 3.7% in 14Q2 and 4.0% in 14Q3. The acceleration in 14Q3 is mainly due to the end of electricity subsidy in June 2014. If we take out this factor, the underlying inflation rate is estimated to be 3.3% in 14Q3.

Unemployment Rate
(Seasonally adjusted)



- The provisional seasonally adjusted unemployment rate improved slightly to 3.1% in the 3 months ending in May 2014 from the 3.2% in the 3 months ending in April 2014. We expect a stable labour market and steady wage growth. The unemployment rate is expected to be jittering at around current full employment level in upcoming quarters. It is forecast to be 3.2% in both 14Q2 and 14Q3. The labour force is estimated reaching 3.9 million persons, with 7000 job creation in current quarter compared to the last quarter.

Concluding Remarks

We lower our forecast of annual growth of real GDP to 3.1% in 2014, as opposed to the 3.5% announced earlier. This revision reflects the unexpected larger impact of the harsh winter in the US which slapped its economy to shrink by an annualize rate of 2.9% in the first quarter of 2014. Nevertheless, the setback in the US recovery is likely temporary. It seems that EU recovery remains on track, China's economic performance remains in check, and the lower interest rate environment will continue for a while. Much uncertainty in the external sectors remains. Taken together, we remain cautiously optimistic about the economic conditions of Hong Kong

About Hong Kong Macroeconomic Forecast Project

The Hong Kong Macroeconomic Forecast is based on research conducted by the APEC Studies Programme of the Hong Kong Institute of Economics and Business Strategy at HKU in the Faculty of Business and Economics. It aims to provide the community with timely information useful for tracking the short-term fluctuations of the economy. The current quarter macro forecasts have been released on a quarterly basis since 1999.

The high frequency forecasting system was originally developed in collaboration with Professor Lawrence Klein of the University of Pennsylvania in 1999-2000. Since then, the system has been maintained and further refined by the APEC Study Center which is now a research programme area of the Hong Kong Institution of Economics and Business Strategy.

The project is sponsored by the Faculty of Business and Economics. The Hong Kong Centre for Economic Research at HKU provides administrative support to the project. Researchers at the Hong Kong Institution of Economics and Business Strategy are solely responsible for the accuracy and interpretation of the forecasts. Our quarterly forecasts can be accessed at:

<http://www.hiebs.hku.hk/apec/macroforecast.htm>

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High Frequency Macroeconomic Forecasts
APEC Studies Programme
Hong Kong Institute of Economics & Business Strategy
The University of Hong Kong

Table 1: Current Quarter Model Forecast
(Millions of 2012 HK Dollar)

	2013					2014		
	Q1	Q2	Q3	Q4	Annual	Q1	Q2 (Estimate)	Q3 (Forecast)
Gross Domestic Product	505,202	498,474	532,056	561,064	2,096,796	517,849	512,780	549,892
Private Consumption Expenditure	337,060	345,329	329,685	359,900	1,371,974	343,962	352,896	339,597
Government Consumption Expenditure	49,666	45,373	47,155	47,422	189,616	50,863	46,734	48,570
Exports of Goods	882,362	929,242	1,006,590	1,010,628	3,828,822	886,385	952,374	1,039,687
Imports of Goods	1,023,170	1,091,541	1,139,956	1,165,175	4,419,842	1,035,605	1,119,790	1,179,333
Exports of Services	253,464	248,669	273,054	282,670	1,057,857	261,195	259,577	286,649
Imports of Services	114,508	108,593	119,145	122,039	464,285	114,304	111,424	122,432
Gross Fixed Capital Formation	115,112	137,594	136,000	145,686	534,392	118,586	135,634	135,473
GFCF in Land & Construction	58,528	53,342	54,963	59,150	225,983	61,184	53,291	53,904
GFCF in Mach., Equip. & Comp. Soft.	56,584	84,252	81,037	86,536	308,409	57,402	82,343	81,569
Changes in Inventories	5,216	-7,599	-1,327	1,972	-1,738	6,767	-3,221	1,682

Date of Forecast: June 27, 2014

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Table 2: Current Quarter Model Forecast
Year-on-Year Growth Rate (%)

	2013					2014		
	Q1	Q2	Q3	Q4	Annual	Q1	Q2 (Estimate)	Q3 (Forecast)
Gross Domestic Product	2.9	3.0	3.0	2.9	2.9	2.5	2.9	3.4
Private Consumption Expenditure	6.3	4.7	2.7	3.6	4.3	2.0	2.2	3.0
Government Consumption Expenditure	1.9	3.1	2.3	2.0	2.3	2.4	3.0	3.0
Exports of Goods	8.8	6.1	6.1	5.7	6.6	0.5	2.5	3.3
Imports of Goods	9.5	7.6	6.6	6.1	7.4	1.2	2.6	3.5
Exports of Services	4.7	7.7	5.0	4.7	5.5	3.1	4.4	5.0
Imports of Services	0.3	-0.7	2.6	5.5	2.0	-0.2	2.6	2.8
Gross Fixed Capital Formation	-3.0	7.6	2.7	5.3	3.3	3.0	-1.4	-0.4
GFCF in Land & Construction	-1.6	-7.4	-3.7	-8.6	-5.4	4.5	-0.1	-1.9
GFCF in Machinery, Equip. & Computer Software	-4.4	19.8	7.6	17.5	10.8	1.4	-2.3	0.7
GDP Deflator Growth Rate	1.8	0.6	1.5	1.5	1.4	2.0	1.6	1.4
CPI (Composite) Inflation Rate	3.7	4.0	5.3	4.3	4.3	4.2	3.7	4.0
Unemployment Rate	3.5	3.3	3.3	3.2	3.3	3.1	3.2	3.2
Date of Forecast: June 27, 2014								

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Table 3: Selected Monthly Indicators
Year-on-Year Growth Rate (%)

	2013			2014								
	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP
Unit Value Trade Index (Domestic Exports)	1.3	0.0	0.5	-0.5	-0.6	-2.0	-1.3	-0.9	-0.6	-0.2	-0.3	0.2
Unit Value Trade Index (Imports of Foodstuffs)	5.7	5.4	4.6	4.7	3.2	3.8	3.7	4.2	3.8	5.3	3.9	3.5
Unit Value Trade Index (Imports of Consumer Goods)	2.6	4.1	2.9	2.9	3.5	3.1	2.7	2.4	2.4	2.2	2.6	1.7
Unit Value Trade Index (Imports of Raw Materials & Semi-Manufactures)	4.1	3.7	3.6	4.4	4.4	3.3	3.0	1.9	1.8	1.5	0.2	-0.9
Unit Value Trade Index (Imports of Fuels)	-3.6	-1.4	0.1	-0.8	-4.8	-3.8	-3.9	-1.5	-0.1	0.6	1.9	-1.8
Unit Value Trade Index (Imports of Capital Goods)	-1.2	-1.8	-2.7	-0.9	1.4	-0.1	0.2	1.6	1.4	0.8	-0.1	0.3
Real Retained Imports of Foodstuffs	4.6	15.8	19.9	-1.6	12.7	-3.9	18.5	12.5	5.4	5.2	3.5	7.8
Real Retained Imports of Consumer Goods	-4.1	-9.3	-6.8	-25.3	37.5	-11.8	-3.8	2.8	5.7	0.1	-5.5	7.1
Real Retained Imports of Raw Materials & Semi-Manufactures	-15.6	0.9	-11.8	12.9	23.2	6.2	34.1	14.4	3.1	19.4	23.2	17.0
Real Retained Imports of Fuels	4.2	3.9	12.6	-0.9	-13.0	-8.7	28.4	5.7	-2.1	13.5	9.6	16.7
Real Retained Imports of Capital Goods	16.0	16.3	29.7	-33.2	28.2	11.8	-6.2	-14.5	-0.5	1.7	-5.2	-5.8
Total Motor Vehicles Newly Registered	18.7	-1.2	17.7	6.9	24.8	-12.1	22.5	15.2	12.8	14.6	17.5	15.4
Private Cars Newly Registered	15.3	-4.5	16.3	-13.3	34.3	-6.5	21.8	11.9	15.6	14.7	19.8	13.7
Money Supply (M2)	12.3	12.5	12.4	9.6	12.8	12.1	12.5	12.7	15.0	14.7	15.3	13.0
Loans and Advances	17.8	17.7	16.0	17.8	21.8	19.0	18.1	18.1	15.6	15.0	14.7	13.3
Volume Index of Retail Sales	5.8	9.0	6.1	16.6	-2.2	-2.5	-9.5	-0.5	-3.5	2.3	2.8	2.2
Visitors Arrivals	9.1	8.6	9.3	17.8	9.8	18.1	10.9	8.5	5.1	10.9	10.4	9.3
Hong Kong Resident Departures	1.0	0.5	-3.8	2.7	-11.0	-12.1	11.7	-1.0	-3.7	3.1	2.8	0.7
Electricity Consumption	0.3	-0.9	-2.2	-1.2	4.3	1.3	3.0	-2.1	-2.3	1.9	-2.2	-0.1
Gas Consumption	7.4	6.7	9.4	6.6	6.4	9.7	2.2	4.2	7.4	5.7	2.5	-0.1
Date of Forecast: June 27, 2014												